



**MONTENEGRO**

**AUDIT AUTHORITY**

No: 3011-4-06-329

Date: December 28<sup>th</sup> 2017

**ANNUAL AUDIT ACTIVITY REPORT**  
**OF THE AUDIT AUTHORITY FOR**  
**IPA COMPONENT IV – HUMAN RESOURCES DEVELOPMENT**

OPERATIONAL PROGRAMME HUMAN RESOURCES DEVELOPMENT 2012-2013

(CCI 2007 ME 05I PO 001)

**FOR THE PERIOD FROM 01<sup>st</sup> OCTOBER 2016**  
**UNTIL 30<sup>th</sup> SEPTEMBER 2017**

Podgorica, December 2017

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## List of abbreviations

AA	Audit Authority
AAO	Annual Audit Opinion
AAAR	Annual Audit Activity Report
AAWP	Annual Audit Work Plan
BROP	Body responsible for Operational Programme
BRPM	Body responsible for Priority/Measure
CFCU	Central Finance and Contracting Unit
CAO	Competent Accrediting Officer
DG EMPL	Directorate General for Employment, Social Affairs and Inclusion
EU	European Union
EC	European Commission
HOS	Head of Operating Structure
IAD	Internal Audit Department
IB	Implementing Body
IPA	Instrument for Pre-Accession Assistance
JD	Job Description
MCS	Management and Control System
MoE	Ministry of Education
MoS	Ministry of Science
MoP	Manual of Procedures
MLSW	Ministry of Labour and Social Welfare
MF	Ministry of Finance
NAO	National Authorizing Officer
NF	National Fund
NIPAC	National IPA Coordinator
OG	Official Gazette
OP	Operational Programme
OS	Operating Structure
OPHRD	Human Resources Development Operational Programme
Rulebook	Rulebook on internal organization and systematization
SoA	Statement of Assurance
WLA	Work Load Analysis

## 1. INTRODUCTION

### 1.1. Operational programme of IPA covered by the report

This report covers the Operational Programme Human Resources Development 2012-2013 (hereinafter Programme or OPHRD) co-financed from the Instrument for Pre-Accession Assistance on Montenegro 2007-2013. European Commission issued Decision C (2012) 7202 on adopting Operational Programme (CCI 2007 ME 05I PO 001) on 18<sup>th</sup> October 2012.

The OPHRD 2012-2013 is divided into four priority axes and the global objective of priority axes shall be implemented through six measures. The total cost of the OPHRD, expressed in terms of eligible public expenditure, is estimated at 6.568.240 EUR (EU Contribution 5.583.000 EUR and National Public Contribution 985.240 EUR). In accordance with Amending the Financing Agreement between The Government of Montenegro and The European Union, represented by the European Commission signed from 24.02.2017, the total cost of the OPHRD 2012-2013, expressed in terms of eligible public expenditure, is estimated at 5.803.344 EUR (EU Contribution 4.932.839 EUR and National Public Contribution 870.505 EUR).

According to the EC Decision (C(2014) 5195) from 28<sup>th</sup> July 2014 on conferring management powers relating to Programme and other adopted documents (Decision No 01-06-5101/1 issued by Ministry of Finance on 09.10.2017) the following structures, bodies and authorities are responsible for the management and implementation of the Programme:

- **National Authorising Officer**, Director General of Directorate of the State Treasury within Ministry of Finance<sup>1</sup> bears overall responsibility for the financial management of EU funds in Montenegro and the regularity and legality of the underlying transactions.
- **National Fund**<sup>2</sup>, within Directorate of the State Treasury in Ministry of Finance, operationally supports.
- **Operating Structure** which encompasses:
  - **Ministry of Labour and Social Welfare** as Body responsible for the Operational Programme and Body responsible for priority axis 1, 3 and 4 and measures in the field of the labour and employment, in particular the measures 1.1, 3.1, 4.1 and 4.2;
  - **Ministry of Education** as Body responsible for priority axis 2 and measures in the field of education, in particular the measure 2.1;
  - **Ministry of Science** as Body responsible for priority axis 2 and measures in the field of research and innovation, in particular the measure 2.2;
  - **Central Finance and Contracting Unit (CFCU)** acting as Implementing Body (Contracting Authority) for all measures implemented within IPA Component IV.

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<sup>1</sup> The function of the NAO was delegated to the State Secretary of the Ministry of Finance which by the Decision of the Minister of Finance has been appointed as NAO on October 9<sup>th</sup> 2017

<sup>2</sup> In accordance with Internal Act on Organization and Systematization of the Ministry of Finance adopted on the Government session held on October 26<sup>th</sup> 2017 National Fund is within Directorate for Management Structure

## **1.2. Bodies involved in the preparation of this report**

This Annual Audit Activity Report has been prepared by the Audit Authority of Montenegro.

The AA of Montenegro, as an independent audit body, was established by the Law on Audit of EU Funds (“Official Gazette of Montenegro” No 14/12, 54/16, 37/17 and 70/17). The AA is responsible for audit of EU funds (IPA, Structural Funds after the accession of Montenegro to the European Union, and other EU funds).

The functional independence of the AA is adequately ensured. According to Article 3 of the Law on Audit of EU funds, the AA is functionally and operationally independent of all actors in EU funds management and control system.

In terms of the organisational setup this means that the AA is set up as a functionally independent body that in no way has any functional relation(s) with the bodies in the operational setup of the management and control system(s) for the execution of EU funded programmes in general and the IPA IV component specific.

The functions of the AA are set out in the Framework Agreement between the Government of Montenegro and the Commission of the European Communities concluded on 15<sup>th</sup> November 2007, and in Commission Regulation (EC) No 718/2007 from 12<sup>th</sup> June 2007 Implementing Council Regulation (EC) No 1085/2006 establishing an instrument for pre-accession assistance (IPA) and other agreements between the European Commission and Montenegro.

The AA is responsible for verifying the effective functioning of the management and control system in the bodies responsible for management and implementation of the OPHRD 2012-2013.

The AA should submit an Annual Audit Activity Report (AAAR) and Annual Audit Opinion (AAO) following the model set out in Annexes C and D of the Framework Agreement, on the basis of the audit activities carried out from 01<sup>st</sup> October 2016 until 30<sup>th</sup> September 2017.

## **1.3. Steps taken for the preparation of the report**

Annual Audit Activity Report (AAAR) is prepared in accordance with the Audit Authority’s Annual Audit Work Plan (AAWP) for period 1st October 2016 – 30th September 2017, which was submitted to the EC-DG EMPL on 29th September 2016, and updated AAWP submitted to the EC-DG EMPL on 3th mart 2017.

The AAAR is prepared as a result of audit activities carried out during the period 01st October 2016 – 30th September 2017. During this period AA carried out system audits, audit of operations and follow-up.

The follow-up was performed as a part of another audit engagement and as a separate activity before issuing the Annual Audit Activity Report and Annual Audit opinion.

In this AAAR the overall overview of audit activities and follow up activities carried out in the above mentioned periods, is provided. The AA prepared the AAAR on its own, taking into consideration that the AA does not rely on the work of other audit bodies in carrying out its functions.

## 1.4. Audit scope

In the period 01st October 2016 – 30th September 2017 AA carried out system audits, audit of operations and follow-up.

### 1.4.1. System Audits

In carrying out the system audits the audit scope was to examine the compliance of the MCS with the requirements set out in the IPA Implementing Regulation No 718/2007, i.e. accreditation criteria provided in the Annex of this Regulation, the Framework Agreement and the requirements set out in other agreements and regulations, and to check whether the established system functions effectively.

During the reporting period auditors have carried out examinations of the effectiveness and efficiency of the management and control systems in auditees. We were focused on the processes/functions/areas listed below and examined their compliance with applicable accreditation criteria.

For the purpose of detailed defining of the scope of the audit, in the planning phase we performed a detailed risk assessment to determine the priority processes in conducting system audits. During the risk assessment, based on gathered documentation, risks were identified and taken into account at the level of each process. Therefore, based on available AA's resources and all collected information and documentation as well as the results of risk assessment, the following audit areas were examined:

- ***Internal organization and Human Recourses*** in Ministry of Labour and Social Welfare; Central Finance and Contracting Unit (CFCU); Ministry of Education; Ministry of Science and National Fund (NF);
- ***Financial Management*** in Ministry of Labour and Social Welfare; Central Finance and Contracting Unit (CFCU); Ministry of Education; Ministry of Science and National Fund (NF);
- ***Internal Audit*** in Ministry of Labour and Social Welfare; Central Finance and Contracting Unit (CFCU); Ministry of Education and National Fund (NF);
- ***IT Policy*** in Ministry of Labour and Social Welfare; Central Finance and Contracting Unit (CFCU); Ministry of Education; Ministry of Science and National Fund (NF);
- ***Contract implementation and OTSCs*** in Ministry of Labour and Social Welfare; Central Finance and Contracting Unit (CFCU); Ministry of Education; Ministry of Science and National Fund (NF);
- ***Programme monitoring*** in Ministry of Labour and Social Welfare; Central Finance and Contracting Unit (CFCU); Ministry of Education; Ministry of Science and National Fund (NF);
- ***Administrative issues*** in Ministry of Labour and Social Welfare (BRPM); Ministry of Education; Ministry of Science;
- ***Contract Procedures, Irregularities, Publicity and Visibility, Communication and Reporting*** in Ministry of Labour and Social Welfare;
- ***Accounting*** in Central Finance and Contracting Unit (CFCU) and National Fund;
- ***Management verifications*** in Ministry of Labour and Social Welfare (BRPM/BRPM);
- ***Statement of assurance*** in National fund (we have reviewed documentation related to issuing SoA by all bodies).

Also, we performed follow up of recommendations given in the previous audit reports. The summary list of the system audits carried out is given in Annex C to this AAAR.

### **1.4.2. Audit of operations**

The audit of operations in the framework of the Operational Programme Human Resources Development 2012-2013 (HRD) has been performed on the operations for which the expenditure were paid and declared to the European Commission (EC) in the period from 1<sup>st</sup> January 2016 until 31<sup>st</sup> December 2016. There was only one statement of expenditure declared to the EC in the period concerned and it was related to the interim payments of three contracts (measures 1.1; 2.1 and 3.1) and direct award within measure 4.2 for technical assistance.

The audit encompassed the expenditure amounting to EUR 460.725,79 which is the 100% of overall declared expenditure.

The following operations and the corresponding expenditure were under the scope of the audit:

- Operation 1.1.1 - Active labour market measures for employability (Priority axis 1);
- Operation 2.1.1 - Modernisation of Educational Programmes and Teacher Training (Priority axis 2);
- Operation 3.1.1 - Cooperation between Employment Agency of Montenegro and Social Work Centres (Priority axis 3)
- Operation 4.2.1 - Supporting Operating Structure in the implementation of the Operational Programme (Priority axis 4).

The following audit areas were covered during the audit of operations:

- a) Operation's compliance with Operational Programme,
- b) Procurement procedures (tendering and contracting),
- c) Eligibility of expenditure,
- d) Publicity and Visibility,
- e) Payments,
- f) Accounting and supporting documents,
- g) National co-financing,
- h) Audit trail.

Following bodies have been covered during the audit:

- Ministry of Finance – Directorate for Finance and Contracting of the EU Assistance Funds;
- Ministry of Labour and Social Welfare - Body Responsible for the Operational Programme (BRBP) and Body Responsible for Priority/Measure 1.1; 3.1 and 4.2;
- Ministry of Education – Body Responsible for Priority/Measure 2.1 and
- National Fund.

### **1.4.3. Follow- up activities**

#### **a) Follow-up as a part of another audit engagement**

During the system audit, the follow-up of findings and recommendations from previous audit(s) was performed, which is then a constituent part of system audit report No 3011-1-06-31/3 from September 6<sup>th</sup> 2017.

## b) Follow-up as a separate activity before issuing the AAAR and the AAO

In December 2017 the AA performed follow-up of the implementation of recommendations from previous audits (audits carried out in 2015 and 2016) and follow up of the findings and recommendations given in the course of audit conducted in the period covered by this report. Follow-up was performed as a separate activity before issuing the AAAR and the AAO and encompassed the following bodies: Ministry of Labour and Social Welfare; Directorate for Finance and Contracting of the EU Assistance Found (CFCU) Ministry of Education; Ministry of Science; and National Fund.

After the Follow-up, in December 2017, we prepared separate Audit Recommendations' Status Reports for each body which is kept in our audit file. For detailed information on our follow-up approach, see Section 5.2 of this AAAR. Results of follow-up activities are described in Section 5.3. and in Section 8 of this report.

## 2. SUMMARY OF FINDINGS

As it was already mentioned in Section 1.4 Audit scope, during 2017 the AA was carrying out system audit, audit of operations and Follow-up of the findings and recommendations given in the course of system audit.

Findings were categorized according to the level of importance to major, intermediate and minor findings.

### 2.1. Summary of findings from system audit

During 2017 System audit has been carried out in all bodies of OS and NF. In late November and during December 2017, as a separate activity, we performed Follow-up of the findings and recommendations given in aforementioned system audit.

The total number of findings in system audit is 15 out of which 10 are intermediate and 5 minor.

For easier review we have prepared the table overview of system findings per audited area/process.

**Table 1:** Number of System findings per audited area/process

Audit Area/Process	Finding (Reference to Section of Report)	MoE	MoS	MLSW BROP/ BRPM	MLSW BRPM	CFCU	NF	Number of findings
Human Resources and Internal Organization	4.1.1			x		x	x	5
	4.1.2	x	x	x	x	x	x	
	4.1.3				x			
	4.1.4				x			
	4.1.5		x					
IT Policy	4.2.1	x	x	x	x	x	x	1
Financial Management	4.3.1	x		x	x			4
	4.3.2					x		
	4.3.3	x	x	x	x	x		
	4.3.4						x	

Internal Audit	4.4.1	x		x	x	x	x	1
Administrative issues	4.5.1				x			3
	4.5.2				x			
	4.5.3		x					
Communication and Reporting	4.6.1				x			1
<b>TOTAL</b>								<b>15</b>

The most of findings were identified regarding: **Human resources and Internal organization** (Understaffing and WLA, Retention Policy, Mismatching between WLA and real state, Insufficient trained staff, Inadequate Substitution plan and Sensitive position); **Financial management** (Verification of timesheet and reports by BRPMs /beneficiaries, Inadequate control of interim reports, “Read and approved” Visa, Payment to contractor); **Administrative issues** (Non-existence of conditions for maintenance of confidential data, Lack of Internal Register Book).

Regarding the **internal organization and human resources** we identified that Retention Policy is not at a satisfactory level. Conducting checks in CFCU and NFD certain deficiencies have been determined referring to: unfilled vacancies, WLA correctness, its compliance with the Rulebook of internal organization and Systematization, lack of one more accountant, etc. When it comes to MLSW (BROP/BRPM and BRPM) we found that there is no sufficient legal basis of one employee in BROP/BRPM for performing certain functions. Deficiencies related to mismatching between the WLA and real state in BRPM are identified. It is evident that only one employee in BRPM mainly has attended all registered trainings. Also, conducting checks in the MoE (BRPM) it is determined that chart relating to organisational structure in MoP is not in compliance with the current Rulebook on internal organisation and systematisation. Auditing this process in the MoS (BRPM) we have found some shortcomings related to Plan for Substitution of Staff and Sensitive position templates.

Given that the human resources is the most important factor for functioning of all systems and taking into consideration the fact that the most of our findings are related to this issue improvements are needed.

Relating to **IT Policy**, we have determined that IPA bodies do not have adequate data backup and employees are not adequately trained concerning nature of threats, virus protection, secure and controllable data storage so there is a significant risk of loss of data. Therefore, data storage is not properly secured and lack of trainings could have a negative effect on the development of competences of employees who should regularly update their knowledge on IT security issues. Bearing in mind previously mentioned, some improvements are needed.

Auditing the process of **Financial management** we have identified some shortcomings, misunderstandings and weaknesses as follows: all reports and timesheets for experts have been approved by Head of BRPM and in some cases by HOS (for measure 1.1.) without appropriate confirmation that the output has been delivered to the Beneficiary/End Recipient although it is noted in MoP that Head of BRPM approves timesheets and provides “Read and Approved” visa only in case when that BRPM is beneficiary, CFCU and BRPMs did not use the annexes for requesting and issuing “Read and Approved” visa which are designed specifically for this issue, certain delays related to payments i.e. transferring of EU funds to the contractors and also certain weaknesses in the control system when checking financial part of interim reports. Bearing this in mind, some improvements are needed.

During the audit of **Internal Audit** function we have identified lack of staff in all bodies. Lack of employees in the Internal Audit Departments, who are in charge of auditing EU funds may affect on performance of tasks as well as quality of conducting the audits. Bearing this in mind, we consider that some improvements are needed.

Auditing the process of **Administrative Issues** we have determined certain deficiencies such as: lack of conditions for storing and keeping documentation with confidential content in MLSW as well as that paper files were not created in compliance with the prescribed procedures; lack of the Internal register book in MoS. Also, during the audit engagement, we have determined mismatching of the chapter Administrative issues and the Financing Agreement. We have reported on this issue during the audits in 2016 and bearing in mind that recommendations regarding this mismatching will be implemented soon, in this audit report we did not put findings regarding this issue. Therefore we think that some improvements are needed.

During our audit engagement in the process of **Communication and reporting** we are convinced that requirements related to: submitting the Quarterly Irregularity report within the defined deadline in MoP, reporting on significant changes and coordination meeting, are mainly fulfilled. However, requirements related to organisation of internal meeting are not fulfilled. Internal meetings were not organised on a regular basis. Bearing this in mind, some improvements are needed.

A detailed description of the principal findings identified and of accompanying recommendations provided, as well as results of follow-up activities are presented in the Chapter 5 - Systems audits (Section 5.3).

A detailed list of all findings, categorised by their level of importance (major, intermediate and minor) is laid down in Annex B to the AAAR.

## **2.2. Summary of findings from audit of operations**

The audit of operations in the framework of the Operational Programme Human Resources Development 2012-2013 (HRD) has been performed on the operations for which the expenditure were paid and declared to the European Commission (EC) in the period from 1<sup>st</sup> January 2016 until 31<sup>st</sup> December 2016. The audit encompassed the operations for which the expenditure in the total amount of EUR 460.725,79 (100% of the overall declared expenditure) was declared to the European Commission (EC).

The audit encompassed the expenditure for four operations. During the audit of operations we have identified one transaction findings – finding which have financial impact.

Based on the audit work performed we have obtained reasonable assurance that the expenditure declared in the amount of EUR 460.725,79 under the audited Operations 1.1.1, 2.1.1, 3.1.1 and 4.2.1 in the reference period 01.01-31.12.2016 is in all material aspects, legal and regular, corresponding to the accounting records and supporting documents, except above mentioned ineligible expenditures.

## **2.3. Conclusion on the functioning of the management and control system for the period ended on 30<sup>th</sup> September 2017**

Our conclusion on the functioning of the management and control system for the period ended on 30<sup>th</sup> September 2017 is based on the audit work carried out during 2017 calendar year. In

that period AA carried out system audit, audit of operations and the follow-up of the findings and recommendations given in the course of system audits. Final System Audit Report was submitted to the EC-DG EMPL on 8<sup>th</sup> September 2017. Also, during 2017 AA continuously monitored the implementation of OPHRD and collected the information on the changes in the system.

We have carried out examinations of the effective functioning of the management and control systems in auditees under the period of performing our audits.

AA has performed System audit in all OS Bodies within Component IV and in NF with the general assessment of MCS - works, but some improvements are needed. We summarized the findings of each body according to the audit area. We also stress the fact that there are no major findings when system audit is concerned. A detailed description of the principal findings identified and of accompanying recommendations provided are presented in the Chapter 5 - Systems audits (Section 5.3).

The audit of operations encompassed the operations for which the expenditure concerns the interim payments and real costs. Conducting Audit of Operations we had aim verifying actual functionality of MCS by checking them directly and provides corroboration of the outcomes of the test of controls (system audits).

During the audit of operations we identified some systemic shortcomings which we also identified in System audit as well as in the previous audit of operations, when recommendations are given for their removal. We also determined transaction shortcomings relating to ineligible expenditure in not so high amount (38,06 €). Regarding that, recommendation relating to recovery of the ineligible expenditure amount has been given.

A detailed description of the shortcomings identified during the audit of operations are presented in the Chapter 6 – Audits of sample of operations.

Based on the audit work performed we have obtained reasonable assurance that the expenditure declared in the amount of EUR 460.725,79 in the reference period 01.01 - 31.12.2016 is in all material aspects, legal and regular, except above mentioned shortcomings.

On the basis of the performed follow-up activities we determined that improvements have been made. Results of follow-up activities related to the principal findings can be found in Section 5.3.

Therefore, on the basis of the work done in the system audit and audit of operations and taking into account the results of follow-up activities we consider that it is appropriate to conclude that the established management and control system for the period 01<sup>st</sup> October 2016 – 30<sup>th</sup> September 2017 functioned effectively and the expenditure declared in the reference period is legal and regular. Consequently, for the period ended on 30<sup>th</sup> September 2017 we will issue an unqualified opinion.

A detailed list of all findings, categorised by their level of importance (major, intermediate and minor) is laid down in Annex B to the AAAR.

### **3. CHANGES IN MANAGEMENT AND CONTROL SYSTEMS**

In our last AAAR we reported on significant changes in the management and control systems (MCS) in the period from 1<sup>st</sup> October 2015 to 30<sup>th</sup> September 2016 and in the period 01<sup>st</sup> October 2016 until mid-December 2016.

#### **3.1. Changes in the MCS since last AAAR**

- **Head of Directorate for Finance and Contracting of the EU Assistance Funds – CFCU**

Ms Marija Radenovic requested from the Government of Montenegro to be dismissed from the General Director. This request was issued at the session of the Government of Montenegro held on 23<sup>th</sup> February 2017. At the same session, Mr Katarina Zivkovic was appointed as the acting General Director of Directorate for Financing and Contracting of the EU Assistance Funds – CFCU. The NAO informed the EC- General Directorate for Employment, Social Affairs and Inclusion about this change on 27<sup>th</sup> February 2017 (letter No 06-1044/1/1).

At the session held on 14<sup>th</sup> September 2017 the Government of Montenegro adopted the Decision on termination of term of office to Katarina Zivkovic acting director of Directorate for financing and contracting of EU funds in the Ministry of Finance (CFCU acting as IB), due to termination of 6 months' period.

At the same session the Government of Montenegro adopted the Decision on appointment of Bojan Paunović as acting director of Directorate for financing and contracting of EU funds in the Ministry of Finance (CFCU acting as IB). The NAO informed the EC on the replacement of General Director of Directorate for Finance and Contracting of the EU Assistance Funds- Letter No 01-17646/1, from October 11<sup>th</sup> 2017.

- **Head of National Fund Division**

By the letter no 06-1044/1 from 27<sup>th</sup> February 2017, NAO informed EC on planned leave of the head of National Fund Division, Ms Dunja Nelević. This job position is vacant from 22<sup>nd</sup> March 2017 until the period covered by this report.

- **Head of BRPM in the Ministry of Education**

Mr Marko Vukasinovic performed the function of the Head of the body responsible for Priority/Measure in the field of education until the 29<sup>th</sup> December 2016 and since then new head of BRPM has been Ms Mubera Kurpejovic, Director General of the Directorate for Higher Education.

#### **3.2. Changes in the MCS from 01<sup>st</sup> October until mid-December 2017**

- **National Authorising Officer (NAO)**

By the Decision no. 01-06-5101/1 from 09/10/2017 the Minister of Finance Darko Radunović appointed Mr Nemanja Katnić – state secretary in the Ministry of Finance as a National Authorising Officer (NAO). EC was informed of this change by letter No. 01-17646/1 from October 11<sup>th</sup> 2017.

- **Organizational changes in the Ministry of finance (NFD)**

At the session of the Government of Montenegro held on 26/10/2017 the Rulebook on internal organisation and systematisation of the Ministry of Finance was adopted. By this Rulebook the new Directorate for management structure consisting of two divisions: Division for National Fund and Division for NAO support is established. National Fund which was within Directorate for State Treasury pursuant to the previous organisation in MF. The NAO informed EC – Directorate General for Neighbourhood and Enlargement Negotiations (copied to DG EMPL) about these organizational changes by letter No.01-21222/1 from 1<sup>st</sup> December 2017.

- **Director General of the Directorate for Management Structure (Deputy NAO)**

By letter No.01-21222/1 from 1<sup>st</sup> December 2017 the NAO, Mr Nemanja Katnić, has informed EC that IPA activities of General Director of the Directorate for Management Structure (Deputy NAO) will be performed by Ms Ivana Maksimovic. Ms Maksimovic is appointed by the Government of Montenegro on November 16<sup>th</sup> 2017 as Acting Director General of the Directorate for Management Structure.

- **Head of Division for National Fund**

By the Decision of the Minister of Finance no. 01-3813/1 from 28/11/2017, Ms Žana Jovanović is assigned to a job position of the head in the Division for National Fund – Directorate for Management Structure.

#### **4. CHANGES TO THE ANNUAL AUDIT WORK PLAN (AAWP)**

Annual Audit Work Plan for the period 01<sup>st</sup> October 2016 – 30<sup>th</sup> September 2017 for IPA Component IV– Human Resources Development, was prepared in September 2016. The Auditor General of Audit Authority approved it and sent to the European Commission with copy to National Authorising Officer on 29<sup>th</sup> September 2016.

In the AAWP we planned system audit in all bodies which participate in management and implementation of IPA Component IV.

According to Audit Authority's Manual of Procedures (Version 2.1) in the context of its audit work, the Audit Authority reports on the basis of work carried out during the period from 01/10/year N to 30/09/year N+1 as at 31/12/year N+1. The audits of operations are carried out on the expenditure declared to the Commission in year N.

By the time of the preparation of AAWP (September 2016), there were no declared expenditures, so in time of preparation of this plan, it was not possible to make detailed plan for carrying out audit of operations.

Bearing in mind, that on 16<sup>th</sup> December 2016, National Authorising Officer submitted Certification of Expenditure and Interim Payment Application to the European Commission, and the note of European Commission - DG Employment (Ref. Ares(2016) 5983765-18/10/2016), AA was updated the AAWP in which we specify approach and audit scope of audit of operations.

In this manner AA updated its AAWP in March 2017 by making detailed plan for carrying out audit of operations for which expenditure were declared in 2016. Updated AAWP was submitted to EC-DG EMPL on 3<sup>th</sup> Mart 2017.

## **5. SYSTEM AUDITS**

This AAAR is prepared by the AA and all activities in the course of 2016-2017 were performed by the AA.

AA had decided to conduct the system audit which encompassed all IPA bodies constituting operating structure for component IV as well as National Fund Division. The list of IPA bodies which were covered by this system audit is given in Annex C to this AAAR.

### **5.1. Basis for selection of the audits**

We performed our activities in accordance with the AAWP for period 01<sup>st</sup> October 2016 – 30<sup>th</sup> September 2017.

During the annual planning, i.e. in September 2016, for the purpose of defining audit areas, the Audit Authority had performed risk assessment for each body of OP HRD at the key requirement/process/function level. The risk assessment was performed on the basis of the information available and current at that time. We identified and assessed issues and processes that were significant for the audit and that could be common for all or several bodies that are participating in management and implementation of operational programme.

Risk factors which were identified and taken into account during risk assessment at the process level for each body were as follows: coverage with the previous audits; results of previous audits; status of implementation of OP HRD 2012-2013; staffing (sufficiency, competence, experience); changes from the previous audits (organizational, procedures, employees); compliance requirements.

In order to distinguish between the factors with varying importance, we gave the weight to the specific risk factors, and calculated the total score for each process level in each IPA body. Finally, we ranked processes in all bodies (organisations) within OP HRD and identified that some processes were high ranked in all (or several) IPA bodies and additional processes which were high ranked only in certain IPA body. So, the result of risk assessment was certain number of common processes for all bodies and certain number of specific processes for each body.

Taking into consideration the above mentioned and available AA's resources, we decided to conduct system audit which included all (five) bodies which participate in management and implementation OP HRD - IPA Component IV as well as NF. This system audit had covered period from last audit engagements in IPA bodies to June 2017.

### **5.2. Follow-up activities**

In accordance with the IPA Framework Agreement, Annex C, Chapter 5 (System Audits) information should be provided on the follow-up of the audit findings. In 2017 AA carried out the follow-up of the findings and recommendations given in the course of previous audits. Consequently, before stating the principal findings and conclusions, recommendations and corrective measures applied, we will briefly describe the follow-up approach of the AA.

According to the AA's Manual of Procedures "The objective of the follow-up process is to determine whether the issues rose in the audit have been adequately addressed and the audit report recommendations are implemented in a timely manner. In general, the follow-up of the audit findings and errors shall be performed annually and the information provided in the Annual Audit Activity Report. The follow-up can be performed as a part of another audit engagement, or as a separate activity before issuing the Annual Audit Activity Report, opinion

(and report) on the management and control systems, and the opinion (and report) on the statement of expenditure. Follow-up by AA is defined as a process by which it determines the adequacy, effectiveness, and timeliness of actions taken by management on reported errors and audit findings, including corrective and preventive measures applied, application of any financial adjustments and remedial action plans. AA should ascertain that actions taken on audit findings remedy the underlying conditions. The same standards for audit evidence shall be applied to follow-up work as those used for documenting original audit work. The results of the follow-up shall be documented in the “Audit recommendation status report”.”

During each individual system audit, the follow-up of findings and recommendations from previous audits is regularly performed, which is then a constituent part of each individual system audit report. Therefore, the follow up as a part of system audit in all OS bodies and NF was performed regarding the findings and recommendations given in system audit reports conducted in these bodies in 2015 and 2016. After receiving the responses and the documentation on the fulfilment of recommendations from all bodies, we conducted interviews with the employees responsible for the management and implementation of the operational programme in bodies in which the interview was needed. After analyses and reviewing the submitted documentation, we assessed the status of the individual recommendation with the respective explanation.

In the period November – December 2017 we performed Follow-up as a separate activity before issuing AAAR and AAO.

For the purpose of carrying out the follow-up we have conducted a set of activities:

- In late November 2017 we sent to all bodies, in which we performed system audit during the previous period, the table with the summary of findings and recommendations from previous audits. We informed them that we need the follow-up for the preparation of the AAAR which should be submitted to the EC, CAO and NAO by the end of December 2017. Therefore, we requested from all the bodies to include into the tables their Management responses on the status of the individual recommendation with the appropriate explanation, regardless of whether deadline for implementation of recommendation has expired or not. We also informed them that they should prepare the evidence on the fulfilment of the individual recommendation which will be provided to us.
- At the beginning of December 2017 we received all the information we requested from all bodies. After receiving the responses and the documentation on the fulfilment of recommendations from all bodies, we conducted interviews with the employees responsible for the management and implementation of the operational programme in bodies in which the interview was needed. Our intention was to discuss certain issues and request additional documentation on the spot, wherever needed.
- After the analysis of the received responses, documentation collected, and interviews conducted, we assessed the status of the individual recommendation with the respective explanation. In mid-December 2017 we prepared a separate Audit Recommendations’ Status Report for each body.

For the system audit which the AA performed in 2017, results of Follow-up activities are described in the section 5.3 of this report.

For the audits carried out in previous period the results of the follow-up are described in Chapter 8 – Follow up of previous year’s audit activity.

### **5.3. Principal findings / Follow-up / Corrective measures applied or recommended and Conclusion**

Further below we outline the description of the most important findings identified and conclusions reached through audit, recommendations provided for correcting the findings as well as information on the measures undertaken for the purpose of resolving the findings with regards to the audited processes and individual bodies and authorities within the system. Conclusions reached through audit and conclusion on the functioning of MCS within OP HRD for period ended on 30<sup>th</sup> September 2017 are given afterwards.

Principal findings (intermediate) identified in the particular audit areas are as follows:

#### **a) Internal Organization and Human Resources**

##### **Findings related to Understaffing and WLA**

Pursuant to the valid Rulebook on Internal Organisation and Systematisation of the Ministry of Finance, 21 job positions are envisaged in the Directorate for Finance and Contracting of the EU Assistance Funds-CFCU and 8 job positions in National Fund Division. The state of human resources in the CFCU is the following: eighteen (18) employees are assigned on the permanent basis and the acting General Director has been appointed – in total nineteen (19) employees, which means that there are two employees less in relation to the current Rulebook. Also, in the valid Rulebook only one job position is foreseen for accountant, which questions “four eyes” principle and also may influence implementation of substitution in an adequate way. In WLA of CFCU the need for 37 employees in total is indicated, which is 16 more than the number of employees which is foreseen in the Rulebook and eighteen (18) more than the current number of employees. Additionally, in WLA draft for 2018 and 2019 it is noted that certain activities (preparing procurement plan and its monthly updates; preparing Payment Plan, Financial checks of invoices/payment claims (administrative) and arrangement of payments) are shown which are related to OP HRD 2012-2013 and which will not be carried out in that period.

In NFD 7 employees are assigned on a permanent basis while the position of Head of NF is vacant. WLA of NFD for 2017 shows that 10 employees are needed which is two more than the number of employees which is foreseen in the Rulebook. Also, when preparing its WLA NFD did not show the current number of employed staff and additionally the gap between the required and the actual number of employees has not been displayed.

Pursuant to the Rulebook on Internal Organisation and Systematisation of the Ministry of Labour and Social Welfare 7 job positions are envisaged in the Division for Programming and Implementation of EU Funds (BROP/BRPM) plus Director General of Directorate for European Integration, Programming and Implementation of EU Funds - acting as HOS.

In the period of performing audit, the state of human resources in the Division for Programming and Implementation of EU Funds is the following: six (6) employees are assigned on the permanent basis and the General Director has been appointed – in total seven (7) employees. The position of Head of Division is vacant.

##### ***Recommendations:***

We recommend to CFCU and NFD to harmonize the number of employees in the Rulebook of internal organization and systematization with needs for staff expressed in WLA, and afterwards filling of necessary vacancies. Also, with a view to carrying out functions undisturbedly and respecting “four eyes” principle in the Accounting of CFCU, it is necessary

to foresee and employ one more accountant.

We recommend to CFCU to carry out corrections in WLA in compliance with the properly foreseen future activities according to all actual Programmes.

We recommend to NFD to update the WLA in a manner that actual number of employees is shown in WLA and accordingly the gap between the required and the actual number of employees is displayed.

In order to ensure effective functioning of the Division for programming and implementation of EU Funds, we recommend to BROP/BRPM to fill the vacancy of the head of the Division.

### ***Results of Follow-up:***

According to new Rulebook on Internal Organisation and Systematisation of Ministry of Finance, National Fund Division is now within new Directorate for Management Structure. This Directorate has two divisions: Division for System Supervision (NAOSO) and National Fund (NF) Division. By newly adopted Rulebook, beside positions of Director General, 2 Heads of the Divisions, 8 positions are predicted within Directorate (more precisely 4 positions within NAOSO and 4 more positions within NF). That means that Directorate will be comprised with 11 state employees what is in line with needs for staff expressed in WLA. Also, by new Rulebook 37 positions are predicted in CFCU according to the WLA. Bearing in mind aforementioned, we consider this recommendation **partially implemented** and we will monitor full implementation.

Recommendations concerning the WLAs of CFCU and NFD, i.e. DMS, are **not implemented**. The implementation of recommendations will be verified.

When it comes to finding and recommendation given to MLSW (BROP/BRPM), actions on implementation of recommendation are undertaken. The vacancy of Head of Division for programming and Implementation of EU funds in MLSW has been filled in November 2017 so we find this **finding closed**.

### **Finding related to Retention policy**

Retention policy shall be based on the Law on Civil Servants and State Employees and aims at ensuring the retention of staff in IPA Body and promoting their effectiveness.

During the audit performed, based on insight into submitted documentation and interviews with employees in IPA bodies, we determined the following:

Technical assistance projects implemented in past few years had direct influence and impact on all employees and provided them with the possibility to raise awareness and gain experiences from countries already implemented stages and processes commenced in Montenegro. A number of trainings, seminars, study visits, workshops have been organised aiming to upgrade professional knowledge and the opportunities for continuing professional development of staff in IPA bodies.

However, we have concluded that the IPA bodies did not use adequate instruments and practical measures for retention of trained staff. Based on insight into staff overviews it is evident that during the last two years certain number of employees left IPA bodies. For example, three employees left CFCU (Head of CFCU, one Quality Assurance Specialist and one Financial Controller). Additionally, one employee (Contract manager) announced plans to resign. In the previous 2 years three employees left NFD.

Bearing in mind previously mentioned, it is evident that human resource policy, including staff retention policy, has not been fully implemented, i.e. bodies constituting IPA structure have not used all possibilities for retention of staff which are included in the process of management and implementation of IPA projects.

***Recommendations:***

Our recommendation is to consider all possible legal solutions to define proper retention and motivation policy and mechanisms in order to retain trained and professional staff.

We recommend to NAO to initiate the consultation meeting with relevant high level authorities which are in charge of implementation of the salary policies in order to find adequate solution for motivating and retaining the employees which are dealing with IPA tasks.

***Results of Follow-up:***

Auditees informed us that NAO and National IPA Coordinator, in consultation with the Minister of Finance, held a meeting to undertake certain steps in finding the best model for retention and motivation policy for IPA staff, i.e. increasing the salaries of IPA employees, which should be further elaborated and harmonized with the legal base. Additionally, beside the financial motivation, training opportunities and carrier development shall also be a part of general motivation and retention policy.

Taking into account these information, we consider that a significant progress is being made towards solving issues regarding retention and motivation policy. However, the implementation of recommendation will be monitored.

***Finding in MLSW (BRPM) related to Insufficient trained staff***

In this phase of implementation of the projects, it is very important to organize trainings of employees for on the spot checks. Also, one of the main preconditions needed to achieve the prevention of irregularities is organization of trainings for the staff so they have adequate knowledge to recognize potential irregularities as well as to report and take appropriate corrective measures in case of detection of irregularities.

Manual of Procedures foresee that all employees are encouraged to attend conferences, seminars and trainings that would enhance their professional skills. By reviewing the Training Register (2015 and 2016) we have found that Head of Body Responsible for Priority/Measure 3.1 did not organize trainings for on the spot controllers at the level of BRPM.

Additionally, we came to the conclusion that employees are not enough trained for the preventing and managing of irregularities. According to the Training Register, only one employee who is not the Irregularity Officer and has attended training related to Irregularities only once.

***Recommendations:***

We recommend to organize the trainings related to on the spot checks and for the preventing and managing of irregularities.

***Results of Follow-up:***

According to the enclosed documentation and conducted interviews we found that employees of BRPM have attended several trainings: training on managing risks and irregularities,

Monitoring Officer attended the implementation workshop for grant beneficiaries. Moreover, Monitoring Officer was present at on the spot checks for 9 grant contracts. We consider this finding **closed**.

**Finding in MoS (BRPM) related to Inadequate Substitution plan and Sensitive position**

During the audit, we carried out an insight into Plan for Substitution of Staff and Sensitive position templates. Audited subject in the template which is related to Plan for substitution of Staff did not foresee the state which matches the actual state of staff in BRPM. Namely, in the column of template “Substitute in case of absence“, in the existing plan it is foreseen that Head of BRPM is replaced by Head of Division for International programmes and EU Integration although it is the same person.

Also, in the template which is related to Sensitive positions in column “positions”, functions of Head of BRPM and Head of Division for Programmes and EU Integration are separately shown although it is the same person.

Data related to substitution and sensitive position were valid in the period when Head of BRPM was Director General of Directorate for Scientific Research Activity. However, by the Decision on appointment of persons responsible for carrying out decentralised and/or indirect management of pre-accession funds of the European Union from 13/11/2015, the Head of Directorate for international programs and EU integration was appointed to the position of BRPM. Thus, Plan for Substitution of Staff drawn up on 20/01/2017 is not applicable while Annex 5 - Sensitive position also does not give clear information related to assessment of sensitive post.

***Recommendations:***

We recommend drawing up of innovated Plan for Substitution of Staff and Sensitive position which will reflect actual state of staff and their functions in BRPM, by which continuous performance of functions and respect of the rule of segregation of duties will be provided.

***Results of Follow-up:***

MoS (BRPM) submitted Substitution plan and Sensitive position which have been updated in accordance with IPA positions within the Directorate for International Programmes and EI and in line with our recommendation. So we consider this **finding closed**.

**b) IT Policy**

**Finding:**

On the basis of performed on-the-spot checks and conducted interviews, we have found that archiving and backup of data is not performed in accordance with prescribed procedures. There is no properly defined back up storage. So, there is a risk of loss of data in case of error in information systems in which information is destroyed by failures or negligence in storage, transmission, or processing. To mitigate the risk of losing data, the staff from IPA bodies use external hard disks and USB disks for archiving data from their computers. They perform this periodically. Previously mentioned external hard disks are stored in the premises of each IPA body. However, archiving data in this way is not secure enough and is not in accordance with prescribed procedures for back up and archiving data which are described in MoP, chapter IT policy.

Also, we have concluded that employees from IPA bodies did not have enough trainings related to IT security policy. During the last two years insignificant number of employees attended few trainings related to cyber security and computer data protection. Bearing in mind the importance of IT security, using file servers, having adequate and secure data storage, employees from IPA bodies should have more trainings with regard to this policy.

### ***Recommendations:***

We recommend providing adequate archiving and back-up of data according to the procedures described in MoP Chapter IT policy in order to prevent data loss or ensure restoring of lost data.

We recommend initiating and providing trainings related to IT Security policy.

### ***Results of Follow-up:***

According to the auditees' responses and on the spot checks it is evident that employees of IPA bodies are aware of existence of risk of losing data, so a certain progress is made and we determined that most of them currently use share folders in order to maintain all relevant data and documents. Also, share folders are backed up on external hard disks on a monthly basis. More permanent solution has been envisaged by procuring the back-up system within the Measure 4.2. of the OP HRD via tender for supply contract.

Auditees informed us that National authorities started with preparation of an individual action plan for the implementation of a framework of 17 baselines of information security, which the national authorities must draw up and the Government of Montenegro must adopt by 31st of December 2017 at the latest. On the basis of this Action Plan relevant indicators and goals will be measured. National authorities are obliged to set up a Steering Committee before the preparation of the action plan to monitor the implementation of the measures specified in the action plan.

As for the IT trainings, the staff members of couple IPA bodies already have attended respective trainings on IT security and relevant issues.

To summarize, compared to the previous period a significant progress is being made towards raising awareness on IT security and providing adequate archiving and back-up of data. Until the lasting solution is provided for this issue, IPA bodies i.e. employees from IPA bodies use all available options to mitigate risk of losing data.

However, this finding remains **open** and we will monitor the full implementation of recommendation.

## **c) Financial Management**

### **Findings related to Verification of timesheets and reports by BRPMs/Beneficiaries**

According to the MoP V5 Part II, Chapter Financial Management, responsibilities of BRPM/Beneficiary is to: 1) Issue "Read and Approved" visa for reports or confirmation of agreement with reports during Steering Committee Meetings – Service Contracts, FWC, Grant Contracts; 2) Countersign the timesheets - Service Contracts, FWC; 3) Countersign the Provisional Acceptance Certificates and the Final Acceptance Certificates – Supply Contracts. Also, in the same chapter of MoP, it is stated that Head of Beneficiary/Head of BRPM approves timesheets by signing them on a monthly basis, confirms agreement with report (inception, progress, interim, final) and provides "Read and Approved" visa to the Head of IB. It is also noted that Head of BRPM approves timesheets and provides "Read and Approved" visa only in case when that BRPM is beneficiary.

Based on the documentation reviewed and interviews performed in CFCU (IB), MLSW (BROP/BRPM and BRPM) and MoE (BRPM), it is determined that timesheets for experts have been approved by Head of BRPM and in some cases by HOS (for measure 1.1.) without appropriate confirmation that the output is delivered to the Beneficiary/End Recipient. According to OIS, for example for measure 1.1, beneficiaries/end recipients of the service contract within this measure are the Ministry of Labour and Social Welfare and Employment Agency of Montenegro (including its local branch offices). Reviewing the documentation related to the implementation of activities from this service contract we found that representatives of MLSW were not present during the implementation of some activities in EAM and its local branches. Also, it is determined that there were no appropriate audit trail that EAM formally informed MLSW about the results of activities on which the representatives from MLSW were not present. However, each reviewed expert's timesheet has been signed and approved by the HOS. So, expert's timesheets within measure 1.1. have not even been signed and approved by the Head of BRPM or Head of Beneficiary but all have been approved by the HOS, which is not acceptable.

The same thing is when it comes to service contracts within measures 2.1 and 3.1. For example, according to the OIS for measure 3.1 beneficiaries/end recipients are the Ministry of Labour and Social Welfare, the Employment Agency of Montenegro (including its local branch offices) and Social Work Centres. Certain activities are predicted and performed only for employees of EAM or only for employees from SWCs. Therefore, there were activities on which only EAM representatives were present, or only SWC representatives i.e. activities on which representatives of MLSW (BRPM) were not present. We have determined that there is no document issued by EAM or SWC concerning the confirmation that activities and trainings which were carried out for their needs are implemented in a proper way and in accordance with special conditions of the contract. And besides that, all expert's timesheets for this service contract have been signed and approved by Head of BRPM (MLSW). Also, in all cases "Read and Approved" visa has been issued by Head of BRPM. Although the EAM and SWCs are beneficiaries/end recipients, until now, they have not formally approved any expert's timesheet or issued "Read and Approved" visa for reports or issued any confirmation of agreement with reports.

To summarize, all reports and its supporting documents have been verified and approved without any formal confirmation by beneficiaries/end recipients that they have actually received services.

### ***Recommendations:***

We recommend verifying the documents related to contract implementation in a manner that each Beneficiary/BRPM verifies the relevant document by which that beneficiary institution confirms that services have been delivered to them.

### ***Results of Follow-up:***

According to the auditees' responses and submitted documentation it is evident that IPA bodies have recognized and understood the essence of the recommendation. So it is for example BROP/BRPM enclosed several confirmations on delivering services which have been issued by beneficiary institutions. Other IPA bodies acknowledged the need for getting the confirmation on the activities presented in experts' timesheets but as service contracts in meantime ended they could not require a proof/confirmation from the beneficiaries involved in projects for those activities.

Therefore, we consider this finding and recommendation have achieved the essence and that is

increasing awareness on need of improving the control system in such a way that each head of beneficiary institution is involved in monitoring the implementation of the project and assumes the responsibility to confirm that certain services have been delivered to his/her institution/employees.

Bearing in mind previously mentioned, we consider this finding **closed** and note that all BRPMs should continue with this practise in next programming period.

### **Finding to CFCU (IB) related to Inadequate control of interim reports**

The IB ensures that all the relevant checks are performed in accordance with article 19 of the Framework Agreement, IPA IR 718/2007, the relevant Financing and Operational Agreements, PRAG and other instructions and guidance provided by the HOS and NAO.”

According to the MoP V5 Part II, IB\_CFCU, Chapter Contract Impl and OTSCs, section 4.3.4 “Interim reports are normally submitted every six month and are the basis upon which an interim payment is made to the contractor. Where quarterly progress reports are required, the previous quarterly progress report will be incorporated into the interim progress report. The content of this report is similar to that of the quarterly progress report but will include a copy of the signed timesheets of the experts and **documentation substantiating any incidental expenditure incurred**. This is to enable the relevant interim payment to be made.”

By reviewing the documentation in CFCU (IB) and MLSW related to approving of interim reports and then executing payments on the basis of these reports, we have identified certain deficiencies. Reviewing the first interim report for service contract within measure 1.1 we have determined that financial part of this report was not complete i.e. did not contain all the documents (invoices/requests for payment/etc.) as a relevant confirmation that incidental expenditures are actually incurred. The auditees have presented a table summarizing the costs for incidentals but we were not presented the documentation substantiating incidental expenditures incurred. Also, while examining the financial part of first interim report for service contract within measure 3.1 we have found that one document (bill for catering services) is not appropriate. Namely, there is no fiscal excerpt from the cash register. This incidental expenditure has been justified with some “type” of a bill which is not acceptable according to the Montenegrin national rules. It is just a hand-written bill on A5 format and with unclear stamp. This type of bill without fiscal excerpt from the cash register is not acceptable.

### ***Recommendations:***

We recommend to improve controls of verification of the financial reports and supporting documents which are submitted by Contractors. The documentation substantiating incidental expenditures incurred should be the integral part of each financial report.

### ***Results of Follow-up:***

According to the response and submitted documentation we are convinced that CFCU has acted upon the recommendation and got all the missing documentation. Also, CFCU informed us that they will request from contractors all documentation substantiating for any incidental expenditure incurred for interim and final payments.

Bearing in mind previously mentioned, we find this finding **closed**.

### **Finding related to Payments to Contractors**

In accordance with Article 5 of Annex A of the Framework Agreement, all payments by the Commission shall be made to an interest bearing euro account, opened by the National Fund in a financial or treasury institution, on behalf of the beneficiary country and under the National Fund's responsibility. The sole authority authorised to request funds from the Commission and to authorise transfers of funds from this account to the operating structure, or any final beneficiary as may be designated by the operating structure, is the National Authorising Officer. In addition article 154 of the Directions on State Treasury Operations (OG MN No. 20/14) defines “Funds for the implementation of the payment request funded by the EU are provided with the transfer from the IPA account to the main account of the state treasury and at the same day the payment is made to the supplier, including part which is funded by the EU as well as the part that is co-funded from national resources”.

During the audit we have identified certain delays (approximately 6-10 days) related to payments i.e. transferring EU funds to the contractors. Namely, during the 2016 and 2017 NF proceeded a number of requests for funds related to the different stage of projects and transferred funds from IPA account “MF-NF IV HRD OP 2012-2013” to the Main Treasury account. In certain number of contracts within OP HRD contractors did not receive funds on the same day when EU part was transferred from IPA account to the main account of the state treasury which is not in line with article 154 of the Directions on State Treasury Operations (OG MN No. 20/14).

#### ***Recommendations:***

National Fund shall ensure that funds – EU part should be transferred to the Contractor account on the same day when they are transferred from IPA Central bank account to the Main Treasury account in line with the Directions on State Treasury Operations (OG MN No. 20/14). In case that specific situation arises and funds are not transferred to the account of supplier, NF should initiate procedure for withdrawal of funds to the IPA account.

#### ***Results of Follow-up:***

Auditee informed us that they have undertaken initial step in order to resolve this issue and harmonize the MoP with the Directions of the State Treasury Operations. They requested by relevant stakeholders to give their opinions on this issue.

Bearing in mind that recommendation is not implemented this finding stated **open**.

#### **d) Internal audit**

### **Findings related to Strengthening internal audit capacities**

According to the Law on Internal Financial Controls in public sector (PIFC), the Internal Audit Department cannot have less than 3 internal auditors with the Head of the Internal Audit Department.

Auditing the function of IAD in all IPA bodies we found that number of staff is not in line with the number of staff envisaged in the Rulebooks of Internal organization and systematization.

For example, according to the valid Rulebook of Internal organization and systematization of Ministry of Finance, seven job positions are foreseen in the Internal Audit Department and according to job descriptions all of them are in charge of auditing EU funds. However, five job

positions are filled while two job positions are vacant. Additionally, Ministry of Finance has signed 17 Agreements on the entrustment of internal audit work. By signing these Agreements IAD is committed to perform internal audit in the institutions with which agreements have been signed, which significantly increases their work load. The WLA for 2017 has shown the necessity for 8 staff member. Taking into account the WLA of Internal audit and the fact that they have signed 17 Agreements on the entrustment of internal audit work, new employees are needed.

The Rulebook of internal organization and systematization of the Ministry of Labour and Social Welfare foresees 4 job positions in the Internal Audit Department: Head of Internal Audit Department, Superior Internal auditor, Senior Internal Auditor and Junior internal auditor. During the audit in the MLSW we found that the Head of Internal Audit Department and Senior Internal Auditor during the April and May 2017 have moved to another job position and that only one internal auditor (Junior Internal Auditor) is employed in the IAD. According to the job descriptions in valid Rulebook, three job positions are in charge of auditing EU funds and all three are vacant.

Also, the Rulebook of internal organization and systematization of the Ministry of Education foresees 4 job positions in total in the Internal Audit Department. It is determined that 3 internal auditors, Head of Internal Audit Department, Superior Internal Auditor and Junior internal auditor, are employed. Job position of Senior Internal Auditor is vacant. According to the job descriptions in Rulebook “Senior Internal Auditor” and “Junior Internal Auditor” are in charge of auditing EU funds. So Internal Audit Department currently can’t perform the audit activities relating EU Funds with full capacities.

When it comes to the Ministry of Science, it is determined that this Ministry does not have internal audit department but internal audit tasks are entrusted to IAD of Ministry of finance.

Lack of employees in the Internal Audit Departments, who are in charge of auditing EU funds may affect on performance of tasks as well as quality of conducting the audits.

### ***Recommendations:***

We recommend strengthening internal audit capacities by filling vacant work posts in the Rulebooks of Internal organization and systematization and also respecting the needs expressed in the WLA.

### ***Results of Follow-up:***

Reviewing the responses and documentation enclosed by MLSW, MoE, NF and CFCU it is evident that certain activities are carried out in respect of stranghtening internal audit capacities. Namely, MLSW engaged one more internal auditor so currently two positions in the MLSW Internal Audit Department are filled: Superior Internal Auditor and Senior Internal Auditor. IAD of Ministry of Finance sent to the Minister Letter on necessity for additional employment and now are expecting the answer. MoE answered that during 2018 it is envisaged that vacancy for one position in Internal Audit Department will be published.

Bearing in mind all previously mentioned it is evident that certain shift regarding this finding was made but findings remained **open** and the implementation of recommendation will be monitored.

#### e) Administrative issues

##### **Finding in Ministry of Labour and Social Welfare (BRPM) related to Non-existence of conditions for maintenance of confidential data**

The Manual of Procedures defines that “Some files of the IPA bodies require confidential treatment (i.e. Tender proposals during evaluation, Irregularities Reports) and they shall be managed within secured restricted environment, observing the following principles: the files must be kept in locked, separated area; log of retrieval of these files must be maintained and access to such files must always be authorized by appropriate officials (NAO, HOS/Head of BROP, Head of BRPM, Head of IB, Irregularity officer, etc.); retention period must be defined, destruction formally approved by responsible officials (NAO, HOS/Head of BROP, Head of BRPM, Head of IB)”.

However, it is determined by the audit that there is no adequate place for maintenance of confidential files in the Division for risk group protection - acting as BRPM for PA3 (lack of lockers with the possibility of locking for safe keeping of confidential documents). Lack of proper equipment for keeping confidential documents may lead to possible loss of confidential and sensitive information.

##### ***Recommendation:***

It is recommended to procure equipment and to create adequate conditions for storing and maintaining documentation with confidential content.

##### ***Results of Follow-up:***

Through follow up activities it has been determined that MLSW (BRPM) purchased one locker for the purpose of storing and maintaining documentation with confidential content. The locker is key protected. However, by purchasing one locker MLSW did not provide all necessary conditions for maintenance of confidential data so we consider this recommendation **partially implemented**. We will monitor the full implementation of recommendation.

## **6. AUDITS OF SAMPLE OF OPERATIONS**

The audit of operations in the framework of the Operational Programme Human Resources Development 2012-2013 (HRD) has been performed on the operations for which the expenditure was paid and declared to the European Commission (EC) in the period from 1<sup>st</sup> January 2016 until 31<sup>st</sup> December 2016. There was only one statement of expenditure declared to the EC in the period concerned and it was related to the interim payments of three contracts (measures 1.1; 2.1 and 3.1) and direct award within measure 4.2 for technical assistance.

In accordance with the AA's audit methodology, during the audit we covered the expenditure amounting to EUR 460.725,79 which is 100% of the total expenditure declared to the EC.

Audit of operations in the course of 2017 was performed by the AA.

The list of the audit of operations carried out is given in Annex D to this AAAR.

Summary data of the audited operations are presented in the following table:

Priority/ Measure/ Operation		Total expenditure declared (EUR)	Union contribution (EUR)	National contribution (EUR)	Expenditure audited (EUR)	Type of payment
<b>Priority Axis 1: Efficient and inclusive active employment policy measures</b>						
<b>Measure 1.1.</b> Supporting the implementation of the most productive labour market measures for the labour force quality and employment	<b>Operation 1.1.1</b> Active labour market measures for employability (Service contract)	194.615,86	165.423,47	29.192,39	194.615,86	<b>Interim payment</b>
<b>Priority Axis 2: Enhancing Skills, Knowledge and Competences for Employability and Competitiveness</b>						
<b>Measure 2.1</b> Supporting the improvement of conditions for development of VET qualifications	<b>Operation: 2.1.1</b> Modernisation of Educational Programmes and Teacher Training (Service Contract)	167.544,66	142.412,91	25.131,75	167.544,66	<b>Interim payment</b>
<b>Priority axis 3: Enhancing Social Inclusion</b>						
<b>Measure 3.1</b> Supporting greater access to labour market for persons with disabilities and RAE population	<b>Operation 3.1.1.</b> Cooperation between Employment Agency of Montenegro and Social Work Centres (Service contract)	81.095,15	68.930,84	12.164,31	81.095,15	<b>Interim Payment</b>
<b>Priority axis 4: Technical assistance</b>						
<b>Measure 4.2</b> Supporting Operating Structure in the implementation of the Operational Programme	<b>Operation 4.2.1</b> Supporting Operating Structure in the implementation of the Operational Programme	17.470,12	14.849,57	2.620,55	17.470,12	<b>Real costs</b>
<b>Total</b>		<b>460.725,79</b>	<b>391.616,79</b>	<b>69.109,00</b>	<b>460.725,79</b>	

## **6.1. Results of the substantive testing**

During the audit of Operations we have identified one transaction finding – finding which have financial impact.

By examining the documentation related to first interim payment for service contract within measure 3.1, we have determined ineligible expenditure within incidental costs. Namely, Contractor made a payment for participants of working groups who were coming to the meetings of the Working group from other places on the territory of Montenegro, inter alia by verifying costs of using their own cars. This cost is allocated to incidental expenditure, and its calculation is carried out in compliance with the Article 25 of the Decree on Expense Reimbursement of Employees in Public Sector (Official Gazette of Montenegro no. No 26/12 from 24/05/2012).

However, having an insight into documentation by which incidental expenditure is verified, we determined that the Contractor had not carried out the calculation by the price for the type of fuel which users actually used, but the calculation had been carried out by the higher price. As an evidence on type and price of fuel, the Contractor delivered to IB fuel bills, but the calculation had not been carried out in accordance with the data on fuel price from those bills.

Thus Contractor along with the first Interim Report presented and requested payment of the increased amount of incidental expenditure of 14,06 €, which was also paid to him. Having in mind the above-described reasons, this expenditure is considered ineligible.

Apart from the above mentioned, Contractor also reported as an incidental expenditure cost related to Costs for logistical organisation of training and workshops activities. By the insight into documentation related to verification of this type of costs, we determined the existence of inadequate receipt which justifies the cost (there is no fiscal receipt of catering services provider). It is the receipt which was allegedly issued by Property Administration on 11/05/2016 at the amount of 24,00 €. Documentation which justifies this cost does not provide enough assurance on actual cost existence, and therefore this amount is also considered ineligible.

Total ineligible incidental expenditure amounts 38,06 €. We have given recommendation to recover amount of ineligible expenditure.

## **7. COORDINATION BETWEEN AUDIT BODIES AND SUPERVISORY WORK OF THE AUDIT AUTHORITY**

The AA does not rely on the work of other audit bodies in performing its functions and responsibilities.

## **8. FOLLOW - UP OF PREVIOUS YEARS' AUDIT ACTIVITY**

Follow-up approach of the AA was in detail described in Section 5.2.

Results of the follow-up for the audits carried out in previous period are described in this Section of the Report. Follow up covered the results of the audits from previous years (2015 and 2016) in MLSW (BROP/BRPM), CFCU (IB), MoE (BRPM), MoS (BRPM) and NF.

We would like to stress that during system audit carried out in 2017 the follow-up on recommendations from previous audits was performed, which is then a constituent part of

system audit report. Also, in December 2017 Audit Authority performed further follow-up of those findings and recommendations and follow up of findings and recommendations from system audit report conducted during 2017, as separate activity before issuing the AAAR and the Annual Audit Opinion (AAO).

Summarized overview of the status of findings identified in previous audits in all bodies of OS and NF which remained open after issuing previous AAAR, is given in table below:

No	Findings identified during the system audits	Level of priority*	Status in Dec 2017	New deadline
<b>Ministry of Labour and Social Welfare (BROP/BRPM)</b>				
1	Inadequate premises (BROP/BRPM)	Minor	Partially implemented	1 <sup>st</sup> Q 2018
2	Verification of tender documentation by HOS/BROP	Intermediate	Open	1st Q 2018
3	Non-existence of conditions for maintenance of confidential data	Intermediate	Partially implemented	1st Q 2018
4	Inadequate description of procedures relating to retention of documents in MoP	Minor	Open	1st Q 2018
5	Non-compliance between flowchart and scheme with described procedures within Chapter Irregularities	Minor	Open	1st Q 2018
6	Annual Implementation Report	Minor	Open	1st Q 2018
7	Back up of data	Intermediate	Open	1st Q 2018
<b>Directorate for Finance and Contracting of the EU Assistance Funds (CFCU)</b>				
1	Written Procedures related to the Irregularities	Intermediate	Open	1st Q 2018
2	Inadequate archiving space	Minor	Partially implemented	1st Q 2018
3	Written Procedures related to Administrative issues	Minor	Open	1st Q 2018
4	Accounting software	Intermediate	Closed	-
5	IT Policy	Intermediate	Open	1st Q 2018
6	Deficiencies in the organization of a coordination meeting at the level of the IB	Minor	Open	1st Q 2018
<b>Ministry of Education (BRPM)</b>				
1	Inadequately presented organizational structure in MoP	Minor	Open	1st Q 2018
2	Inadequate job description	Minor	Closed	-
3	Unfilled vacancies in the Internal Audit Department	Intermediate	Closed	-
4	Non-compliance between flowchart and scheme with described procedures within Chapter Irregularities	Minor	Open	1st Q 2018

<b>Ministry of Science (BRPM)</b>				
1	Inadequate Job Description in the Rulebook of the Ministry of Science and inadequate description in the MoP	Minor	Open	1st Q 2018
2	Absence from Risk Panel	Intermediate	Closed	-
3	Non-compliance of flowchart and scheme with described procedures within Chapter Irregularities	Minor	Open	1st Q 2018
4	Assignment of the Publicity Officer	Minor	Open	1st Q 2018
<b>NATIONAL FUND (NF)</b>				
1	Preparation of Statement of Assurance	Intermediate /Minor	Closed	
2	Incompatibility of decisions on employment with the Rulebook on internal organization and systematization	Minor	Closed	
3	Written Procedures related to the Irregularities	Intermediate	Open	1st Q 2018
4	Written Procedures related to Administrative issues	Minor	Open	1st Q 2018
5	Internal Control weaknesses	Minor	Open	1st Q 2018
6	Business continuity plan	Intermediate	Open	1st Q 2018
7	Lack of holding internal meetings at the level NFD	Minor	Closed	

<b>No</b>	<b>Findings identified during the audit of operations</b>	<b>Level of priority*</b>	<b>Status in Dec 2017</b>	<b>New deadline</b>
<b>Directorate for Finance and Contracting of the EU Assistance Funds (CFCU)</b>				
1	Lack of agreements between OS and end recipients	Major	Closed	-
2	Tender opening session	Intermediate	Closed	-
3	Responsibilities of the Evaluation Committee members	Intermediate	Closed	-

Based on the follow-up activities performed relating to the findings identified in system audits from previous years it is determined that 7 (25%) recommendations out of 28 were implemented, 3 (about 11 %) was partially implemented and 18 (64%) not implemented. Thirteen out of these eighteen findings which remained open is related to deficiencies within written procedures.

Regarding the finding number 1 in MLSW, we emphasize that first part of finding related to premises is closed. As for the adequate equipment, it has been envisaged to procure the adequate equipment within the Measure 4.2. of the OP HRD via tender for supply contract. The tender was re-launched in November 2017 and the OS is still waiting for the outcome of the evaluation. Via the same tender procedure OS plans to procure adequate lockers for maintenance of confidential data (finding number 3 in MLSW and finding number 2 in CFCU).

## **9. RESOURCES USED BY THE AUDIT AUTHORITY**

The AA carried out all audits in 2017 with its own resources.

Rulebook on internal organization and systematization of the Audit Authority, which was adopted in November 2016 foresees four organizational units as follows:

- 1) Department for audit of the program – building institutions and strengthening capacities; social and economic and regional development; employment, social policies, education, promotion of gender equality and development of human capacities;
- 2) Department for audit of the program of the regional and territorial cooperation;
- 3) Department for audit of the program of agriculture and rural development;
- 4) Administrative and Professional Service of Audit Authority.

The audit engagements in 2017 have been implemented by five auditors.

## ANNEX A: ANNUAL WORK PLAN FROM 01<sup>st</sup> OCTOBER 2016 UNTIL 30<sup>th</sup> SEPTEMBER 2017

AAWP for the period from 01<sup>st</sup> October 2016 until 30<sup>th</sup> September 2017 was prepared and submitted to the EC and NAO in September 2016. In this respect, overview table of planned audit activities containing activities planned in period 01<sup>st</sup> October 2016 – 30<sup>th</sup> September 2017 are enclosed in the attachment.

NO	NAME OF THE AUDIT (AUDIT OBJECT) /AUDIT ACTIVITY	OBJECTIVE OF THE AUDIT	AUDITEE	INDICATIVE DEADLINE OF THE AUDIT REPORT AND AUDIT TIMING	AUDIT TYPE	REMARKS
1	Audit of operations	Verify the legality and regularity of expenditure and the reliability of accounting information provided to the Commission	Bodies within the MCS in OPHRD	September- November 2016	Audit of operations	Completion of audit of operations commenced in July 2016 (AAWP 2015-2016)
2	System audit of the Management and control system of the Operating structure of IPA Component IV and National Fund	Verify whether the established MCS in the OS bodies and NF is in accordance with requirements set in IPA Implementing Regulation, Framework Agreement and Financial Agreement whether these established systems functions effectively.	Ministry of Labour and Social Welfare– BROP/BRPM 1& 4; Ministry of Labour and Social Welfare – BRPM; Ministry of Education- BRPM; Ministry of Science- BRPM; CFCU – IB; National fund/NAO.	January – May 2017	System Audit	On the basis of the results of risk assessment the following processes will be audited: Human Resources Management and Internal organization; IT Policy; Financial management; Contract Implementation and OTSC and Programme monitoring (last two processes refer to bodies within OS); Contract procedures; Irregularities; Publicity and visibility; Communication and reporting (for BRPM 3); Administrative issues (in BRPMs); Management verifications(BROP); Accounting (IB and NF)
3	Audit of operations	Verify the legality and regularity of expenditure and the reliability of accounting information provided to the Commission	Bodies within the MCS in OPHRD	June - September 2017	Audit of operations	-

OTHER ACTIVITIES						
4	Follow-up	Follow-up of previous audits AA's for the purposes of issuing the AAAR and AAO	Ministry of Education-BRPM; Ministry of Science-BRPM; Ministry of Labour and Social Welfare – BROP/BRPM; CFCU and NF		Follow-up	Follow-up of previous audits AA's for the purposes of issuing the AAAR and AAO
5	Reporting (AAAR and AAO)	Preparing AAAR and AAO for OP within IPA Component IV		Reporting (AAAR and AAO)	Preparing AAAR and AAO for OP within IPA Component IV	
6	Planning (AAWP)	Preparing AAWP for OP within IPA Component IV for the following reference year (1.10. 2017–30.09.2018)		Planning (AAWP)	Preparing AAWP for OP within IPA Component IV for the following reference year (1.10.2017–30.09.2018)	

\* COMMON BODIE FOR COMPONENT IV AND OTHER IPA COMPONENTS – Considering that National Fund participate in the implementation of IPA Components III and IV, it is planned to perform joint audit by the relevant Units in the Audit Authority.

Abbreviations used in the Table:

MCS – Management and Control Systems

OP – Operational Programme

HOS – Head of Operating Structure

AAWP-Annual Audit Work Plan

BROP - Body responsible for the Operational Programme

BRPM - Body responsible for Priority/Measure

IB - Implementing Body

AAAR-Annual Audit Activity Report

AAO - Annual Audit Opinion

MCS - Management and Control Systems

CFCU –Central Financing and Contracting Unit

## ANNEX B: LIST OF FINDINGS FROM SYSTEM AUDITS AND AUDIT OF OPERATIONS

In accordance with Chapter 2 - Summary of Findings, a List of findings is provided regarding single report on the system audits and audit of operations:

No	FINDINGS IDENTIFIED DURING THE HORIZONTAL SYSTEM AUDIT	Priority level	Reference to Section of Report
1.	Understaffing and WLA (CFCU, MLSW, NF)	Intermediate	4.1.1
2.	Retention Policy (all bodies)	Intermediate	4.1.2
3.	Mismatching between WLA and real state in MLSW (BRPM)	Minor	4.1.3
4.	Insufficient trained staff of MLSW (BRPM)	Intermediate	4.1.4
5.	Inadequate Substitution plan and Sensitive position in the MoS (BRPM)	Intermediate	4.1.5
6.	IT Policy (all bodies)	Intermediate	4.2.1
7.	Verification of timesheets, reports, etc. (BRPMs)	Intermediate	4.3.1
8.	Inadequate control of interim reports (CFCU)	Intermediate	4.3.2
9.	“Read and Approved” visa (all bodies except NF)	Minor	4.3.3
10.	Payments to Contractors (NAO/NF)	Intermediate	4.3.4
11.	Strengthening internal audit capacities (all bodies except MoS)	Intermediate	4.4.1
12.	Non-existence of conditions for maintenance of confidential data in MLSW (BRPM)	Intermediate	4.5.1
13.	Inadequate management document system in MLSW (BRPM)	Minor	4.5.2
14.	Lack of Internal Register Book in MoS (BRPM)	Minor	4.5.3
15.	Lack of holding internal meetings at the level BRPM (MLSW)	Minor	4.6.1

No	FINDINGS IDENTIFIED DURING THE AUDIT OF OPERATIONS	Priority level	Reference to Section of Report
1.	Transaction finding: Ineligible expenditure within incidental costs (CFCU)	Major	2.1

**ANNEX C: SUMMARY LIST FOR SYSTEM AUDITS CARRIED OUT FROM 01<sup>st</sup> OCTOBER 2015 UNTIL 30<sup>th</sup> SEPTEMBER 2016**

Date of performance of the system audit	Programme / system audited	Auditing entity	Expenditure declared in reference year EUR	Total cumulative expenditure declared EUR	Basis of selection of the programme <sup>3</sup>
February - June 2017	OPHRD CCI 2007 ME 05I PO 001	<ul style="list-style-type: none"> <li>➤ Directorate for Finance and Contracting of the EU Assistance Fund (CFCU)- IB;</li> <li>➤ Ministry of Labour and Social Welfare – HOS, BROP/BRPM;</li> <li>➤ Ministry of Labour and Social Welfare – BRPM;</li> <li>➤ Ministry of Education – BRPM;</li> <li>➤ Ministry of Science – BRPM;</li> <li>➤ National Fund (NF).</li> </ul>	460.725,79	990.066,39	Risk Assessment

<sup>3</sup> Within IPA Component IV there is one programme Operational Human Resources Development 2012-2013 Risk assessment was performed in purpose of determining the priorities in conducting system audits through bodies participating in the management and implementation of IPA Component IV.

**ANNEX D: SUMMARY LIST FOR DECLARED EXPENDITURE AND SAMPLE AUDITS CARRIED OUT FROM 01<sup>st</sup> October 2016 UNTIL 30<sup>th</sup> September 2017**

Fund	Reference (CCI no)	OP	Expenditure declared in ref. year	Expenditure in ref year audited for the random sample		Amount and percentage (error rate) of irregular expenditure in random sample (3)		Other expenditure audited (4)	Amount of irregular expenditure in other expenditure sample	Total expenditure declared cumulatively	Total expenditure <i>audited</i> cumulatively as a percentage of total expenditure <i>declared</i> cumulatively	Materiality level (%)	Confidence level (%)
				1.	2.	Amount	%						
	<b>CCI2007 ME05I PO 001</b>	<b>HRD</b>	<b>460.725,79</b>	<b>460.725,79</b>	<b>100%</b>	<b>38,06</b>	<b>0,0083</b>	<b>0,00</b>	<b>0,00</b>	<b>990.066,39</b>	<b>100%</b>	<b>2%</b>	<b>/</b>
	/	/	/	/	/	/	/	/	/	/	/	/	/
	/	/	/	/	/	/	/	/	/	/	/	/	/